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CHARLES ELMORE CROP

IN THE

Supreme Court of the United States

OCTOBER TERM, 1946.

No. 565

FAIRFIELD STEAMSHIP CORPORATION,

Petitioner,

—against—

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, AND BRIEF IN SUPPORT THEREOF.

FRANK V. BARNS,
Counsel for Petitioner.

THE COURT PRESS, N. Y. C.

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IN THE

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OCTOBER TERM, 1946.

No. .

FAIRFIELD STEAMSHIP CORPORATION,
Petitioner,

—against—

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Fairfield Steamship Corporation, the Petitioner, respectfully prays that Writ of Certiorari issue to review a judgment of the United States Court of Appeals for the Second Circuit, entered on June 21, 1946 (R. 150), affirming a decision of the Tax Court of the United States. Petition for Rehearing denied July 8, 1946 (R. 158-159).

OPINIONS BELOW.

The Opinion of the Tax Court (R. 32-36) (Judge Disney) is reported 5 T. C. 65.

Dissenting opinion (R. 36-38) (Judge Arundell) is reported 5 T. C. 65. Judges Fossan and Murdock agreed with the dissent (R. 36-38).

The Opinion of the Circuit Court of Appeals for the Second Circuit (R. 144-148) (before L. Hand, Augustus N. Hand, Clark, *Circuit Judges*) not yet reported. Decided June 21st, 1946.

Petition for Rehearing denied, July 8th, 1946 (R. 158-159).

An Addendum to Opinion of the Circuit Court was dated August 9th, 1946 (R. 149).

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered July 8th, 1946. Petition for Rehearing denied July 8, 1946 (R. 158). Jurisdiction is conferred upon this Honorable Court by Section 240 (a) of the Judicial Code, as amended by the Act of February 13th, 1925.

Summary Statement of the Matter Involved.

The questions at issue here arose out of the efforts of the Executors of the Estate of Arthur R. Lewis, deceased, to liquidate certain corporations which Mr. Lewis had financed and incorporated, and which were part of his estate.

Among the corporations were Atlantic Coast Shipping Company, Inc., and the Petitioner, Fairfield Steamship Corporation.

In 1940, all of the stock of Atlantic Coast Shipping Company was owned—51 percent by Arthur R. Lewis, Jr.; 39 percent by Lewis and Barns, Executors of Lewis's Estate, and 10 percent by a Mrs. Dennis. Atlantic Coast Shipping Company, Inc., owned all of the stock of Fairfield Steamship Corporation.

Fairfield's only assets consisted of the ss "Maine", and some cash.

The three shareholders of the Atlantic Coast Shipping Company in the summer of 1940, and even earlier, had agreed upon a liquidation of Atlantic Company, and of Fairfield Company.

It was agreed that Fairfield Company would be liquidated by transferring the ss "Maine", and all other assets of the Fairfield Company to Atlantic Company in exchange for all of the stock of Fairfield Company.

During the summer of 1940, the ss "Maine" was under charter for a voyage to South and East Africa, and she was expected to return to the Port of New York and go off charter in late September.

Formal meetings of the stockholders of Atlantic and Fairfield were held on September 19th, 1940, authorizing the transfer of the assets of Fairfield to Atlantic in exchange for all of the stock of Fairfield Company.

The ss "Maine" did return to the Port of New York on September 20th, 1940. On September 23rd, Fairfield Company gave a bill of sale of the ss "Maine" to Atlantic Company; the bill of sale was recorded at the Customhouse in Baltimore on September 26th, 1940.

On September 30th, 1940, Atlantic entered into a written contract with Glover Bros. for the sale of the ss "Maine".

Application was made to the Maritime Commission to transfer the ss "Maine" to Glover Bros. and to British Registry, the approval of the Maritime Commission having been obtained, Atlantic on October 3rd, 1940, transferred the ss "Maine" to Glover Bros. in accordance with the terms of sale entered into on September 30th, 1940.

In its 1940 income and declared value excess profits tax return, Atlantic reported a long term capital gain of $331,726.85, as a result of the sale of the ss "Maine".

Fairfield did not report any gain for Federal tax purposes from the sale of the ss "Maine".

The majority opinion of the Tax Court held that the executed sale of the ss "Maine" was in substance the sale of Fairfield.

Among other findings of fact, the Tax Court found:

"Early in September 1940, and prior to September 13, 1940, Lewis asked Charles C. Pendleton (hereinafter referred to as Pendleton), who was executive vice president of Seas,* to see what kind of an offer he could get for the 'Maine'. Pendleton got in touch with Sylvester J. Lambert (hereinafter referred to as Lambert), a broker, who had previously sold ships on behalf of the Lewis interests and with whom Pendleton spoke almost daily. Pendleton requested Lambert, about September 9, to get the best price he could obtain on the vessel, advising him that there was a possibility of selling the 'Maine' after certain formalities were taken care of. Although Pendleton knew, he did not tell Lambert that it was contemplated that any sale of the 'Maine' would be made by Atlantic and not by Fairfield, which was the owner of the vessel at the time of this conversation. Lambert never knew who the title owner of the 'Maine' was until September 30, 1940.

On September 9, 1940, Lambert, who knew that the British Government was in the market to pur-

* Reference to "Seas" was a reference to Seas Shipping Company, Inc., an operating steamship company, of which Arthur R. Lewis, Jr., was, and is, President.

chase ships, addressed a letter to E. P. Rees, Director of the British Ministry of War Transports, also called the British Ministry of Shipping, which provided in part as follows:

'We are authorized by the owners of the American S. S. "Maine" to submit this vessel to you for purchase and solicit your best firm offer. She is presently operating, however, is expected light at a North of Hatteras port between September 25th/30th * * *.'

Rees ascertained about September 1, 1940, as a result of consulting Lloyd's Register that the owner of the 'Maine' was listed there as Fairfield.

On September 11, 1940, Lambert orally received a firm offer from Rees on behalf of the British Ministry to purchase the 'Maine' at $45 per deadweight ton subject to certain conditions. Lambert thereupon on September 11, 1940, wrote the following letter to Pendleton:

'We are authorized by The British Ministry of Shipping to make you a firm offer for the purchase of the Steamer "Maine" on the following terms:

$45 per deadweight ton
10% deposit to be paid in escrow on signing contract, the balance on delivery against bill of sale
Subject transfer flag without restriction
Delivery, North of Hatteras at port where there is no sales tax in effect
September 20th/October 10th
Otherwise terms of British Ministry form of Contract, copy of which was sent you under separate cover.'

"Pendleton communicated this offer to Lewis who told him that the offer was unsatisfactory; that he should try to get a better offer; and that they were not in a position to sell the 'Maine' because title to it was then held by Fairfield; and that any sale of the 'Maine' would be made by Atlantic. Pendleton told Lambert that the offer of $45 would not be acceptable and Lambert suggested that he would try to get a better offer.

A few days after September 11, 1940, Rees orally renewed the offer for the 'Maine' on behalf of the British Ministry at $47.50 per deadweight ton, subject to the same conditions. Lambert conveyed this second offer to Pendleton who reported it to Lewis. Pendleton and Lewis decided to try to get more than $47.50 for the 'Maine'. Pendleton thereupon told Lambert that the offer was not acceptable and that Lambert should try to get a better price. Lambert asked Pendleton to make a counter-offer, but Pendleton replied that they would not be in a position to make any counter-offer until certain formalities in the office took place. The declination of this offer was communicated to Rees.

On September 18, 1940, Rees orally made an offer through Lambert for the 'Maine' at $50 per deadweight ton on the condition that a reply be received not later than 5 p. m. on September 10, 1940. Lambert orally communicated the offer to Pendleton, who relayed it to Lewis without advising the latter of the time limit. Lewis told Pendleton that the price was all right, but that the sale of the vessel would not be accomplished until after September 19, 1940, on which day appropriate corporate action would be taken by the stockholders of Atlantic and Fairfield to effect a transfer of title to the 'Maine' from Fairfield to Atlantic. Pendleton told Lambert that the offer would be acceptable, but that nothing could be done until the vessel had been

transferred to Atlantic, as he was not authorized to accept on behalf of Fairfield. Lambert, prior to 5 p. m. on September 18, 1940, advised Rees that the offer was accepted. Also, on September 18, 1940, Rees received a cable from London which read in part as follows:

> 'You may negotiate "Maine" but as vessel apparently closed shelter deck consider fifty dollars excessive and forty-seven point fifty should be equivalent to this type of vessel.'

Rees replied to that cable the night of September 18, 1940, as follows:

> '"Maine": Were under offer at $50 prior receipt your 1021 (reference is to cable quoted above) which owners have accepted * * * expect delivery Baltimore early October period (R. 24-27).'"

The majority opinion of the Tax Court states:

"All of the facts convince us that this is a case of conduit utilized by the original owner, Fairfield, to route the property to the purchaser after an arrangement so complete as to be considered by the purchaser as binding. Under such facts, and after the expression of the Supreme Court in the Court Holding Co. case (*Commissioner* v. *Court Holding Co.*, 324 U. S. 331) that lack of execution of contract by the corporation (Fairfield) is unimportant, if the sale is in substance the sale of the corporation (Fairfield), we may not give effect to the contention that no firm offer was accepted by Fairfield. We think it was accepted in substance by Fairfield by its conduit Atlantic, if not earlier. Lewis, the same man who governed the matter in accepting for Atlantic, governed the rejection (in effect only until after the transfer) by Fairfield. Such a rejection amounted, in substance, to accept-

ance, except that another (the conduit or nominee Atlantic) would carry out the agreement" (R. 34).

The majority of the Tax Court concluded that their decision was proper under *Commissioner* v. *Court Holding Co.* (supra).

The minority opinion on the same facts found that the Court Holding case involved an entirely different situation, and that the profits from the sale were taxable only to Atlantic.

On appeal to the Circuit Court of Appeals, that Court said "it is impossible to find support in the record for a finding that the Fairfield made the sale, and if that was the legal result of what they did, it was imposed upon the transaction in spite of their intent" (Opinion, C. C. A., R. 147).

The Circuit Court of Appeals also said:

"We think that her transfer to Atlantic Company on September 23, resulted in a gain taxable against the Fairfield Company, because it was neither a 'distribution' 'in complete cancellation or redemption of all its stock' under Sec. 112 (b) (6) (C), nor 'one of a series of distributions' under Sec. 112 (b) (6) (D). Section 112, as a whole, provides for the suspension of what would otherwise be immediately 'realized' gains or losses; it has its reason and its justification in the fact that the excepted transfers are of a kind which do not result in substantial changes of interest, and that the original business is to go along as before. * * *.

* * *. But it does mean that the privilege assumes that the business shall continue and that the liquidation shall not be merely a step in winding it up" (R. 147-148).

On or about August 15th, 1946, counsel for Petitioner received a printed copy of the decision of the Circuit Court of Appeals with an Addendum dated August 9th, 1946. The Addendum is as follows:

> "Our statement that the transfer of the ship to the Atlantic Company 'resulted in a taxable gain against the Fairfield Company' because it was not within Sec. 112 (b) (6) (C) or Sec. 112 (b) (6) (D), was elliptical and may cause confusion. All complete liquidations effect a dissolution of the corporation, although all dissolutions are not liquidations within the meaning of Sec. 112 (b). Although for the reasons we gave, the transfer of the ship, followed in December by a transfer of other assets, was not a 'liquidation', it nevertheless completed a dissolution of the Fairfield Company; and in such cases 'the corporate existence is continued for the purpose of liquidating the assets and paying the debts'. The Atlantic Company, which occupied the position of receivers or trustees in dissolution, stood 'in the stead of the corporation for such purposes. * * *. Any sales of property by them are to be treated as if made by the corporation for the purposes of ascertaining the gain or loss.' Regulations 103, Sec. 19.22-(a)21" (R. 149).

All of the material facts were found by the Tax Court and by the Circuit Court. The Petitioner accepts those findings.

The Circuit Court has affirmed an Order of the Tax Court affirming a deficiency assessment against the Petitioner, and at the same time, it is respectfully submitted, has brought about by and through its decision a state of confusion making it impossible for a taxpayer to know, or the Bar to advise as to the tax obligations, and the benefits to be derived under Section 112 of the Internal Revenue Code.

REASONS RELIED ON FOR ALLOWANCE OF THE WRIT.

1. The Circuit Court of Appeals has erred in holding that in order to have a non-taxable transfer under Section 112 (b) (6) (C) or Section 112 (b) (6) (D), the parent company receiving the property of the subsidiary must continue the business of the subsidiary.

2. The Circuit Court of Appeals erred in holding that a transfer by a subsidiary to a parent company of all of the property of the subsidiary in complete cancellation or redemption of all of the subsidiary's stock is not a distribution in complete liquidation under Section 112 (b) (6) (C) where the transfer is made merely as a step in liquidating the subsidiary.

3. The Circuit Court of Appeals erred in holding that the parent corporation acted as a receiver or trustee for its subsidiary.

4. The Circuit Court of Appeals erred in holding that the transfer of the property to Atlantic Company resulted in a taxable gain to the Fairfield Company.

5. The Circuit Court of Appeals erred in basing its conclusions that the sale of the property was governed by Regulations 103, Sec. 19.22-(a)21.

WHEREFORE, your Petitioner respectfully prays that a Writ of Certiorari be issued out of and under the seal of this Honorable Court directed to the Circuit Court of Appeals for the Second Circuit, commanding that Court to certify and send to this Court for its review and determination on a day certain to be therein named, a full and complete transcript of the record and all proceedings in the Case No. 222, Octo-

ber Term, 1945, and entitled Fairfield Steamship Corporation, Petitioner, vs. Commissioner of Internal Revenue, Respondent, to the end that said case may be reviewed and determined by this Court as provided by law; that the determination of the United States Circuit Court of Appeals for the Second Circuit, may be reversed, and that your Petitioner may have such other and further relief as may be just.

FAIRFIELD STEAMSHIP CORPORATION,
By: FRANK V. BARNS,
Counsel for Petitioner.

Dated: New York, N. Y., September 30, 1946.

Certificate.

I hereby certify that I have examined the foregoing Petition, and in my opinion it is well founded and entitled to the favorable consideration of the Court, and that it is not filed for the purpose of delay.

FRANK V. BARNS,
Counsel.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1946.

No. .

FAIRFIELD STEAMSHIP CORPORATION,
Petitioner,

—against—

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

Statement of the Case.

A summary statement of the case, and of the opinions of the Courts below, and the basis of jurisdiction of this Court, and the reasons relied upon for allowance of the writ are contained in the Petition at pages 2 to 10, and they are not repeated here.

CONGRESS ENACTED THE INTERNAL REVENUE CODE FOR THE PURPOSE OF FIXING THE TAX LIABILITIES OF TAXPAYERS. WHEN THE LOWER COURTS RENDER DECISIONS WHICH NULLIFY THE INTENT OF CONGRESS, AND WHICH MAKE THE FUTURE APPLICATION OF A PART OF THE ACT UNPREDICTABLE, THIS COURT SHOULD EXERCISE ITS POWER TO PREVENT CONFUSION AND TO SAFEGUARD THE RIGHTS OF BOTH THE GOVERNMENT AND TAXPAYERS.

I.

The Circuit Court of Appeals erred in holding that the transfer of the ss "Maine" to the Atlantic Company was not a distribution in complete cancellation or redemption of all of its stock under Section 112 (b) (6) (C) of the Internal Revenue Code.

Section 112 of the Internal Revenue Code in part is as follows:

> "SEC. 112. RECOGNITION OF GAIN OR LOSS.
>
> (b) * * *.
>
> (6) PROPERTY RECEIVED BY CORPORATION ON COMPLETE LIQUIDATION OF ANOTHER.—No gain or loss shall be recognized upon the receipt by a corporation of property distributed in complete liquidation of another corporation. For the purposes of this paragraph a distribution shall be considered to be in complete liquidation only if—
>
> * * *.
>
> (C) The distribution is by such other corporation in complete cancellation or redemption of all its stock, and the transfer of all the property occurs within the taxable year; in such case the adoption by the shareholders of the resolution under which is authorized the distribution of all the assets of such corporation in complete cancellation or redemption of all its stock, shall be considered an adoption of a plan of liquidation, even though no time for the completion of the transfer of the property is specified in such resolution; or
>
> (D) Such distribution is one of a series of distributions by such other corporation in complete

cancellation or redemption of all its stock in accordance with a plan of liquidation under which the transfer of all the property under the liquidation is to be completed within three years from the close of the taxable year during which is made the first of the series of distributions under the plan, except that if such transfer is not completed within such period, or if the taxpayer does not continue qualified under subparagraph (A) until the completion of such transfer, no distribution under the plan shall be considered a distribution in complete liquidation.

* * *."

The Petitioner accepts the facts as found by the Tax Court and by the Circuit Court of Appeals.

Petitioner was unwilling to accept the conclusions of law of the Tax Court that the sale of the "Maine" was in substance the sale of Fairfield Company, and that such a conclusion was under *Commissioner* v. *Court Holding Company,* 324 U. S. 331.

On appeal to the Circuit Court of Appeals, the Court said:

> "The three shareholders of the Atlantic Company in the summer of 1940, and even earlier, had agreed upon a liquidation of that company and of the Fairfield Company at the same time. However, it was from the first intended that the ship would be sold by the Atlantic Company after title to it had passed upon the liquidation of the Fairfield Company. * * *" (R. 145-146).

The Circuit Court of Appeals disagreed with the Tax Court's interpretation of the *Court Holding* case.

Commenting upon the majority opinion of the Tax Court, the Circuit Court of Appeals said:

> "A majority of the Tax Court thought, because the negotiations had been concluded by a satisfactory offer before the Fairfield Company transferred the ship, that the sale was to be imputed to that company. They did not hold, and indeed they could not properly have held, that as a matter of fact the shareholders of the Atlantic Company ever meant the Fairfield Company to sell the ship; on the contrary the shareholders had most carefully provided the contrary. Thus, so far as the transaction depended upon the actual intent of the only parties who could have any intent, it is impossible to find support in the record for a finding that the Fairfield Company made the sale; and if that was the legal result of what they did, it was imposed upon the transaction in spite of their intent. The case is further complicated by the fact that the majority relied for their decision upon an interpretation of *Commissioner* v. *Court Holding Co.*, 324 U. S. 331, to which we cannot agree" (R. 146-147).

The Circuit Court of Appeals did not reverse, and expressed its embarrassment in disturbing any decision of the Tax Court. (It must be assumed it had the case of *Dobson* v. *Commissioner of Internal Revenue*, 320 U. S. 489 in mind.)

The Circuit Court, having found that the definite plan of the shareholders of Atlantic Company had been formulated and agreed upon early in 1940, and that it was from the first intended that the ship would be sold by Atlantic after title had passed to it upon liquidation of Fairfield, it is respectfully submitted that the transfer was one in complete liquidation of the

Fairfield Company and under Section 112 (b) (6) (C) did not result in any gain recognizable against Fairfield Company.

The Circuit Court did not make this conclusion of law, but stated that it was not a distribution in complete cancellation or redemption of stock under Section 112, and the Court said further:

> "Section 112, as a whole, provides for the suspension of what would otherwise be immediately 'realized' gains or losses; it has its reason and its justification in the fact that the excepted transfers are of a kind which do not result in substantial changes of interest, and that the original business is to go along as before" (R. 147).

The Petitioner respectfully submits that nothing was done or left undone upon which the Circuit Court of Appeals could properly deny to the Petitioner the substantial rights given it by the enactment of Section 112 of the Internal Revenue Act, and it asks this Court to reverse the final orders of the Tax Court, and the Circuit Court of Appeals affirming a deficiency assessment against the Fairfield Steamship Corporation.

The Circuit Court of Appeals has by its decision nullified the intent of Congress expressed in Section 112, and has left taxpayers and the Bar unable to determine whether a non-taxable transfer may be made as a step taken by a parent company to liquidate a subsidiary company; and whether it is necessary for the parent company receiving the property of the subsidiary to continue in business, and if so, for what length of time. Certainly the plain language of Sections (C) and (D) do not indicate that the parent company must continue business.

There is an existing state of confusion and the Bar can only turn to this Court and ask it to decide whether the Statute is to be construed and followed in accordance with the plain words in which it was enacted, or whether taxpayers and the Bar must continue with a multitude of cases and the uncertainty of the outcome.

The Circuit Court of Appeals in its decision stated—"The situation seems to be like that in *Gregory* vs. *Helvering,* 293 U. S. 465". That case did not involve a distribution made upon complete liquidation of a corporation, but involved a reorganization under Section 112 (g) of the Revenue Act of May 29th, 1928. There, a corporation was created having no business or corporate purpose. The sole purpose was to consummate a transfer of corporate assets to the petitioner and not to reorganize a business or any part of a business, and was as this Court stated—"an elaborate and devious form of conveyance masquerading as a corporate form of reorganization".

In the instant case, Atlantic had been engaged in business for many years. It had owned all of the stock of Fairfield Company and when Fairfield transferred its property to Atlantic in process of liquidation, there was no change of interest. It did not do it as a mere matter of form, but the real substance of the entire transaction was the carrying out of a definite plan of liquidation of both companies, and in the way provided for in Section 112 to effect a nontaxable transfer and avoidance of double taxation.

The original stockholders of Atlantic had the right to have incorporated the Fairfield Company for the purpose of owning and operating a merchant vessel, the ss "Maine", and to be protected against the hazards of steamship operation. We submit that it

was the purpose of Section 112 to make it possible for those who invested in corporate businesses and enterprises to liquidate a corporation business when the time came to discontinue business.

After the decision was rendered under date of June 21st, 1946, the Petitioner filed its Petition for a Rehearing (R. 152-157). This Petition was denied on July 8th, 1946, without opinion (R. 158-159).

On or about August 15th, 1946, counsel for the Petitioner received by mail the printed copy of the decision of the Circuit Court of Appeals with the Addendum dated August 9th, 1946 added to the original decision, in the form contained in the original record certified by the Circuit Court of Appeals at pages 144-149 of the record. This seemed an unusual procedure. Apparently in the Court's opinion it was necessary to dissipate confusion introduced by its original opinion. This Addendum was issued after the Mandate had issued from the Circuit Court of Appeals.

It is respectfully submitted that the Addendum does not clarify, but leaves the logic and effect of the original decision and the Addendum still more difficult to follow.

II.

The Circuit Court of Appeals erred in holding that Atlantic, the parent company, acted as Receiver or Trustee for its subsidiary, and the transfer of the property resulted in a taxable gain to Fairfield.

Considering all the facts found by either the Tax Court or the Circuit Court of Appeals, we are still without any explanation as to why Atlantic should be held to be acting as a Receiver or Trustee. The

Addendum refers to Regulations 103, Sec. 19.22-(a) 21. Quoted below is Regulations 103, copied from Prentice-Hall Federal Tax Service for the year 1940, under paragraph 7279.

> "REG. 103, Sec. 19.22 (a) 21. GROSS INCOME OF CORPORATION IN LIQUIDATION.—When a corporation is dissolved, its affairs are usually wound up by a receiver or trustees in dissolution. The corporate existence is continued for the purpose of liquidating the assets and paying the debts, and such receiver or trustees stand in the stead of the corporation for such purposes. (See Sections 274 (Par. 19,602) and 298 (Par. 19,262).) Any sales of property by them are to be treated as if made by the corporation for the purpose of ascertaining the gain or loss. No gain or loss is realized by a corporation from the mere distribution of its assets in kind in partial or complete liquidation, however, they may have appreciated or depreciated in value since their acquisition. But see section 44 (d) (Par. 6602) and section 19.44-5 (Par. 6726). (See further section 19.52-2 (Par. 17,280).)"

In view of the facts as found by the Tax Court, and by the Circuit Court of Appeals, the Petitioner is unable to follow the Court's conclusion that Atlantic Company was at any time acting as a Receiver for, or Trustee of, Fairfield Company, and it is respectfully submitted that the tax liability of Fairfield cannot in any way be fixed by Regulations 103.

It is submitted that the conclusions reached in the Addendum are still elliptical.

Even if the facts warranted the conclusions where officers of a corporation (not stockholders) continued

for the purpose of liquidating the assets, and if it be conceded that Regulations 103 is applicable, then one must insert the language of the Regulation which the Circuit Court of Appeals seems to have referred to only by its asterisks:

> "No gain or loss is realized by a corporation from the mere distribution of its assets in kind in partial or complete liquidation, however, they may have appreciated or depreciated in value since their acquisition."

Conclusion.

This case is one concerning questions of utmost importance regarding the construction to be given to Section 112 of the Internal Revenue Code. The limitations which have been imposed upon taxpayers by the decision of the Circuit Court of Appeals are confusing and without Congressional authority. The specific limitations or similar ones have not been passed upon by this Court. An early decision definitely construing the rights of the Government and of taxpayers is of pressing importance, not only to the parties to this case, but also to the multitude of taxpayers who have tax questions involving this Statute.

Respectfully submitted,

FRANK V. BARNS,
Counsel for Petitioner.

Dated: New York, N. Y., September 30, 1946.

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CHARLES ELMORE

IN THE

Supreme Court of the United States

OCTOBER TERM, 1946.

No. 565.

FAIRFIELD STEAMSHIP CORPORATION,
Petitioner,

—against—

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

REPLY BRIEF FOR THE PETITIONER.

The Respondent has filed a brief in opposition to the Petition for a Writ of Certiorari.

The Respondent's brief in its argument in opposing the granting of a writ is based entirely upon Respondent's contention that this case is controlled by the decision of this Court in *Commissioner* v. *Court Holding Company,* 324 U. S. 331.

The Petitioner, in asking this Court to grant a writ of certiorari disagreed with the majority of the Tax Court in applying the *Court Holding* case to the facts of this case, and this position was clearly supported by three dissenting members of the Tax Court. The Circuit Court of Appeals in its decision definitely stated that it could not agree with the Tax Court that the principles laid down in the *Court Holding* case were applicable to the facts in this case.

It is obvious that the Petitioner here would be financially benefitted by a favorable decision of this Court should this petition be granted, and this Court renders a decision in Petitioner's favor. It was not the financial interest of this Petitioner alone which moved this Petitioner to urge the application for the Writ. The Petitioner feels, and it is respectfully submitted that a real question of general public interest is involved.

This case must be governed by the facts. Other cases may have the controlling facts similar, or may in some respects differ. By the decision of the Circuit Court of Appeals, taxpayers and the bar find themselves without definite principles to guide them in transactions relating to non-taxable transfers. It is impossible to determine the rights of taxpayers where Statutory provisions may be materially changed or nullified by the Department of Internal Revenue in its effort to collect taxes.

We all know that as long as we have taxes, the taxpayer will seek to lessen his burden, and the Government will seek to make a maximum collection, but under circumstances such as are presented, not only in this case, but in every case where the question of non-taxable transfer is concerned, we ask and urge that this Court grant the petition for a writ, review the Statute and the subject matter, and lay down some workable principles to be followed so that justice may be done not only to the taxpayer, but to the Government.

Respectfully submitted,

FRANK V. BARNS,
Attorney for Petitioner.

WINTHROP O. COOK,
Of Counsel.

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In the Supreme Court of the United States

OCTOBER TERM, 1946

No. 565

FAIRFIELD STEAMSHIP CORPORATION, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Tax Court (R. 21–36) is reported at 5 T. C. 566. The opinion of the circuit court of appeals (R. 145–150) is not yet reported.

JURISDICTION

The judgment of the circuit court of appeals was entered on June 21, 1946 (R. 151–152). Taxpayer's petition for rehearing was denied on July 8, 1946 (R. 159). The petition for a writ of certiorari was filed on October 4, 1946. The jurisdiction of this Court is invoked under Sec-

tion 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the court below erred in sustaining the Tax Court's decision that a sale, formally made by taxpayer corporation's sole stockholder, was in substance a sale by taxpayer, the gain from which was includible in taxpayer's gross income as defined by Section 22 (a) of the Internal Revenue Code.

STATUTE AND REGULATIONS INVOLVED

Internal Revenue Code:

> SEC. 22. GROSS INCOME.
>
> (a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *. (26 U. S. C. 22.)

Treasury Regulations 103, promulgated under the Internal Revenue Code:

> SEC. 19.22 (a)–19. *Sale of capital assets by corporation.*—If property is acquired

and later sold for an amount in excess of the cost or other basis, the gain on the sale is income. If, then, a corporation sells its capital assets in whole or in part, it shall include in its gross income for the year in which the sale was made the gain from such sale, computed as provided in sections 111 to 113, inclusive. If the purchaser takes over all the assets and assumes the liabilities, the amount so assumed is part of the selling price.

* * * * *

SEC. 19.22 (a)–21. *Gross income of corporation in liquidation.*—When a corporation is dissolved, its affairs are usually wound up by a receiver or trustees in dissolution. The corporate existence is continued for the purpose of liquidating the assets and paying the debts, and such receiver or trustees stand in the stead of the corporation for such purposes. (See sections 274 and 298.) Any sales of property by them are to be treated as if made by the corporation for the purpose of ascertaining the gain or loss. No gain or loss is realized by a corporation from the mere distribution of its assets in kind in partial or complete liquidation, however they may have appreciated or depreciated in value since their acquisition. But see section 44 (d) and section 19.44–5. (See further section 19.52–2.)

STATEMENT

The facts, summarized from the Tax Court's findings (R. 22–32), are as follows:

Atlantic Coast Shipping Company, Inc. (hereafter called "Atlantic") owned all of the stock of taxpayer corporation and 62% of the stock of Cuban Ports Terminal Company (hereafter called "Cuban"). The stock of Atlantic was in turn owned 51% by one Lewis, 39% by Lewis and his attorney as executors of Lewis' father, and 10% by one Dennis. Lewis was president, treasurer, and a director of all three corporations. The offices and books of each corporation were kept at the same address. Taxpayer corporation owned and operated the steamship "Maine", its only other assets consisting of cash and receivables. Atlantic was in the stevedoring business and had never owned any ships. Cuban's only substantial asset was a wharf at Havana (R. 22–23, 29).

Early in 1940, the stockholders of Atlantic agreed upon a tax-saving plan which contemplated the following steps: (1) liquidation of taxpayer corporation; (2) sale of the "Maine" by Atlantic at a profit, as soon as title to the ship was passed to it upon liquidation; (3) disposition at a loss of the wharf owned by Cuban, resulting in worthlessness of Cuban's stock held by Atlantic; (4) offset by Atlantic of the expected gain from the sale of the "Maine" against the ex-

pected worthless stock loss; and (5) liquidation of Atlantic (R. 23–24). Pursuant to this plan and on September 9, 1940, Lewis (acting through one Pendleton) employed one Lambert, a ship broker, to solicit purchase offers for the "Maine". Between September 9 and September 18, Lambert negotiated with British interests and procured two successive offers of purchase. Lewis rejected both, requesting a better price. Lambert renewed his negotiations and on September 18 procured a third and better offer at $50 per deadweight ton. Lewis advised him that this latest offer was acceptable, but that the sale would not be consummated until title to the "Maine" was first transferred from taxpayer corporation to Atlantic. Lambert then advised the purchaser that its latest offer was accepted and that delivery was expected in early October (R. 24–27).

The following day, September 19, a special meeting of Atlantic's stockholders was held at which it was resolved that Atlantic surrender taxpayer's stock in exchange for all of taxpayer's assets, including the "Maine". This meeting was recessed and special meetings of taxpayer's stockholder and directors were then held at which it was resolved that Lewis be authorized to take all steps necessary to dissolve taxpayer. Upon conclusion of these meetings and on the same afternoon, the recessed meeting of Atlantic's stockholders was reconvened, and it was resolved that

Lewis be "authorized to negotiate a contract for the sale of the ss 'Maine', to a prospective British purchaser, at a purchase price of $50. per deadweight ton", and to execute all necessary documents to carry out the sale (R. 27–29).

On September 23, Lewis, as president of taxpayer, executed a bill of sale of the "Maine" to Atlantic, which was recorded September 26. On September 30, Lewis, as president of Atlantic, executed a contract for the sale of the "Maine" to the purchaser. The written contract of sale embodied the same conditions as those specified in connection with the original offer. Delivery was made on October 3, and Lambert received a commission, paid by Atlantic, for procuring an acceptable offer. On December 27, taxpayer transferred to Atlantic the balance of its assets, including $107,855.07 in cash, in exchange for its outstanding stock. The wharf owned by Cuban was sold at a loss (R. 29–31).

In its 1940 income tax return, taxpayer did not report any gain from the sale of the "Maine". In its return, Atlantic reported a long-term capital gain of $331,726.85 from the sale of the "Maine", and a long-term capital loss of $390,000 based upon the alleged worthlessness of Cuban's stock, or a net long-term capital loss of $58,273.15 (R. 31–32). The Tax Court sustained the Commissioner's determination that the sale was in substance that of taxpayer and that the gain was

therefore attributable to it, not to Atlantic (R. 32–36). The circuit court of appeals affirmed (R. 146–150), and denied taxpayer's petition for rehearing (R. 159).

ARGUMENT

This case is controlled by the decision of this Court in *Commissioner* v. *Court Holding Co.*, 324 U. S. 331. There is no occasion for further review.

1. The question here is the same as in *Commissioner* v. *Court Holding Co., supra,* namely, whether the gain from a post-liquidation sale formally executed by a controlling stockholder is attributable to the liquidating corporation or to the stockholder. The long-standing regulations under Section 22 (a) of the Internal Revenue Code, *supra,* provide that if a corporation sells appreciated assets it is taxable on the resultant gain, but that the corporation realizes no taxable gain if it distributes the assets in kind in partial or complete liquidation. Sections 19.22 (a)–19 and 19.22 (a)–21 of Treasury Regulations 103, *supra.* In relieving the corporation of tax liability upon a liquidation distribution of appreciated assets, the statute is patently aimed at genuine distributions in liquidation; it was not intended to embrace one which, though technically perfect, is but a transitory tax-avoidance step in the passage of ownership from the corporation to a

purchaser already found upon terms of sale already agreed upon. In the *Court Holding* case, this Court held (p. 334) that the tax consequences flow from the "substance" of the transaction "viewed as a whole", not solely from the means employed to transfer title to the purchaser; and that whether the sale is in substance that of the controlling stockholder or the corporation presents a question for the Tax Court, whose inference is entitled to finality if supported by evidence. The decisions of the circuit courts of appeals are to the same effect.[1]

Applying the principles of the *Court Holding* case, the Tax Court viewed the instant transaction in its entirety and concluded (R. 32–35) that what substantially occurred was a sale of the steamship "Maine" by taxpayer to a third party via its sole stockholder, Atlantic, not a true liquidation distribution of the vessel and independent sale by Atlantic. The facts found by the

[1] *Mearer Steel Barrel Co.* v. *Commissioner*, 144 F. 2d 282 (C. C. A. 3d), certiorari denied, 324 U. S. 860; *Embry Realty Co.* v. *Glenn*, 116 F. 2d 682 (C. C. A. 6th); *S. A. MacQueen Co.* v. *Commissioner*, 67 F. 2d 857 (C. C. A. 3d); *Trafford Oil & Gas Co.* v. *Commissioner*, 78 F. 2d 814 (C. C. A. 3d), certiorari denied, 296 U. S. 630; *Liberty Service Corp.* v. *Commissioner*, 77 F. 2d 94 (C. C. A. 3d); *Nace Realty Co.* v. *Commissioner*, 28 B. T. A. 467, affirmed *per curiam* April 13, 1935 (C. C. A. 6th); *Boggs-Burnam & Co.* v. *Commissioner*, 26 B. T. A. 988, affirmed, 71 F. 2d 999 (C. C. A. 6th); cf. *Trippett* v. *Commissioner*, 118 F. 2d 764 (C. C. A. 5th), certiorari denied, 314 U. S. 644; *Commissioner* v. *Falcon Co.*, 127 F. 2d 277 (C. C. A. 5th).

Tax Court, and accepted by taxpayer (Pet. 15), unquestionably warrant that inference. Here, as in the *Court Holding* case, the so-called liquidation distribution was effected and the sale consummated by the stockholder only after the purchaser had been solicited and all the material terms of sale had been negotiated. Atlantic's sale was not a new and separate transaction, unrelated to the prior negotiations, but the culminating step of a single business deal. Indeed, the only purchase offer which Atlantic accepted was that submitted and found acceptable while taxpayer owned the vessel, and the formal sale contract which Atlantic executed embodied substantially the same terms of sale theretofore negotiated (R. 24–30, 33–34). Again here, as in the *Court Holding* case, the intervening liquidating distribution served no business purpose but only that of tax avoidance. It was planned from the outset that the gain from the sale would be reported by Atlantic, and offset by its deduction of an alleged worthless stock loss (R. 23–24, 36). Not a single practical result could possibly have been achieved by the circuitous routing of title to the purchaser through Atlantic which would not also have been reached had taxpayer simply and directly consummated the sale itself, collected the purchase price, and distributed the cash proceeds to Atlantic in liquidation. Atlantic did not take title to the "Maine" in order to hold or use the vessel as its own, for ad-

mittedly it immediately re-transferred the title to the purchaser and itself liquidated. Nor could the mechanics employed have facilitated Atlantic's own liquidation, for, had taxpayer directly consummated the sale, Atlantic would have ended up with cash for distribution to its own stockholders—precisely as it did by substituting itself as the vendor.[2]

Affirmance of the Tax Court's decision by the court below was plainly in keeping with established principles, reiterated by this Court in the *Court Holding* case, governing the scope of judicial review of Tax Court decisions.

2. It is true, as taxpayer asserts (Pet. 15–16), that the court below purported to distinguish the *Court Holding* case from this one. It did so on the ground that there the intervening liquidation distribution was contrived as a tax-saving step after the sale negotiations had been completed, whereas here that step was planned from the very start of the negotiations (R. 148). This distinction is one of factual pattern, however,

[2] The unreality of the so-called liquidation distribution is emphasized by the fact that, although taxpayer resolved on September 19 to transfer "all of its assets" to Atlantic "in exchange for all of the outstanding stock" of taxpayer (R. 28, 35), only the "Maine" was transferred to Atlantic on September 23 (R. 29), ostensibly to enable the latter to execute the contract of sale on September 30. Taxpayer's remaining assets (including a substantial amount of cash) were not transferred to Atlantic, nor was taxpayer's stock canceled, until the close of the taxable year (R. 31).

rather than of applicable principles. The "substance" of the transaction depends of course on what was done, not on when the plan for its accomplishment was conceived; nothing in this Court's opinion in the *Court Holding* case or elsewhere warrants the assumption that what is otherwise a single transaction for tax purposes is to be subdivided into its component steps because those steps were contemplated long in advance of their execution. Since "the transaction must be viewed as a whole, and each step, from the commencement of negotiations to the consummation of the sale, is relevant" (*Commissioner* v. *Court Holding Co.,* 324 U. S. at 334), the existence of a preconceived tax-saving plan rather lends cumulative support to the Tax Court's inference that the negotiations for the sale, the transfer of title to the stockholder by way of the so-called liquidation distribution, and the retransfer of title by the stockholder to the purchaser were not isolated transactions, but were interrelated parts of one transaction. Cf. *Commissioner* v. *Tower,* 327 U. S. 280; *Gregory* v. *Helvering,* 293 U. S. 465; *Meurer Steel Barrel Co.* v. *Commissioner,* 144 F. 2d 282 (C. C. A. 3d), certiorari denied, 324 U. S. 860. The court below tacitly acknowledged that the distinction it drew was not a vital one by proceeding to hold (R. 148) that the Tax Court's decision was "right, regardless of whether the shareholders of the Atlantic Com-

pany always intended that that company should sell the ship". And that the rationale of its opinion is essentially, though not expressly, the same as that of this Court in the *Court Holding* case is apparent from its assimilation of this case with the *Gregory* case, upon which this Court relied in the *Court Holding* case.[3]

3. Section 112 (b) (6) of the Internal Revenue Code, with whose provisions taxpayer contends it complied (Pet. 10, 14–19), has no bearing on whether the gain from the sale is includible in its gross income under Section 22 (a). Section 112 (b) (6) deals exclusively with the tax liability of the *distributee stockholder* in certain cases of complete liquidation of a subsidiary by a parent corporation, and represents an exception to the general rule, contained in Section 115 (c), governing the tax consequences to a recipient stockholder upon a liquidation distribution. See Section 19.112 (b) (6)–1 of Treasury Regulations 103. In considering the applicability of Section 112 (b) (6), the court below perhaps attached

[3] Both the reorganization provisions involved in the *Gregory* case and the liquidation-in-kind provisions here involved are aimed at relief from taxation. In both instances no gain or loss is recognized. In neither case does a ritualistic compliance with the literal terms of the relief provisions suffice to give the taxpayer tax advantages that were plainly intended for others. To grant the relief in this case would pervert the purpose of the liquidation-in-kind provisions in the same manner that the taxpayer unsuccessfully sought in the *Gregory* case to misuse the reorganization provisions.

undue significance to the circumstance that the transferee stockholder in this case was another corporation rather than (as in the *Court Holding* case) an individual. Irrespective of whether the recipient stockholder is an individual subject to tax on the distribution under Section 115 (c) or a corporation qualifying for exemption under Section 112 (b) (6), the tax consequence to the *liquidating corporation* in cases like the present turns on whether the liquidation distribution is a real one falling within the purview of the provisions of Section 19.22 (a)–21 of Treasury Regulations 103, *supra,* or an artificial one designed to insulate the corporation from realization of gain on a sale of its assets. This is the transcendent question to which the Tax Court addressed itself, and which it decided adversely to taxpayer. Since its determination has solid evidentiary support, affirmance of its decision by the court below was clearly correct. That in sustaining the Tax Court the court below may have strayed beyond the issue furnishes no basis for further review.[4]

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[4] In the addendum to its opinion (R. 149–150) the court below properly shifted its attention from Section 112 (b) (6) to Section 19.22 (a)–21 of the Regulations, applicable to Section 22 (a). Taxpayer's contention (pet. 19–21) that it was error to consider this regulation is untenable. *Commissioner* v. *Court Holding Co.*, 324 U. S. at 332, note 3; *Hellebush* v. *Commissioner*, 65 F. 2d 902 (C. C. A. 6th); *Tazewell Electric Light & Power Co.* v. *Strother*, 84 F. 2d 327 (C. C. A. 4th); *Northwest Utilities Securities Corp.* v. *Helvering*, 67

CONCLUSION

Taxpayer does not and cannot assert conflict with any decision of this Court or of any circuit court of appeals. To permit the tax consequences here to turn on the considerations stressed by taxpayer would sanction the very type of formalism which this Court has repeatedly refused to recognize as effectual to alter tax liability. The petition for a writ of certiorari should be denied.

Respectfully submitted.

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OCTOBER 1946.

F. 2d 619 (C. C. A. 8th), certiorari denied, 291 U. S. 684; *Taylor Oil & Gas Co.* v. *Commissioner*, 47 F. 2d 108 (C. C. A. 5th), certiorari denied, 283 U. S. 862; *First Nat. Bank of Greeley, Colo.* v. *United States*, 86 F. 2d 938 (C. C. A. 10th). Since the record does not disclose whether taxpayer had satisfied its debts before making the so-called liquidation distribution, its stockholder must in any event be deemed to have acted as trustee in dissolution within the meaning of the regulation, and not in its own behalf, in transferring taxpayer's principal asset to a purchaser and receiving the proceeds. This is consonant with the familiar equity principle that dominant stockholders, by virtue of their fiduciary position, may not deal with the corporate assets as their own. *Pepper* v. *Litton*, 308 U. S. 295, 306–307. Cf. *United States* v. *Joliet & Chicago R. Co.*, 315 U. S. 44, 48–49.

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